Soviet Hard Currency Situation, Trends, and Debt

The USSR's hard currency position has deteriorated steadily since 1984 with its hard currency trade surplus dropping from $4.4 billion in 1984 to under $1 billion in 1985. Hard currency exports declined by 17 percent last year to $26.4 billion--the lowest level since 1979--largely as a result of reductions in the value of oil and arms exports. Moscow countered the earnings decline through increased borrowing and gold sales which allowed it to hold import cuts to 5 percent. Sizable Soviet commercial borrowing coupled with the depreciation of the dollar increased Soviet debt by $6.2 billion to $26.4 billion. At the same time, Moscow rebuilt its assets held in Western banks from a low of about $8 billion at the end of March 1985 to $12 billion by the end of December--about $2 billion higher than at the end of 1984.

Soviet hard currency export earnings have remained depressed through the first half of this year as a result of sharply reduced oil prices. Although total exports of $11.6 billion in the first half of this year were comparable to the level of $11.5 billion in the first half of 1985, this was accomplished, in part, by a 25 percent hike in the volume of oil delivered. Nonetheless, the value of oil exports for the year is likely to drop about $4 billion.

Moscow's response to date has been similar to last year's but with a greater emphasis on import cuts. Hard currency imports totaled $12.9 billion through June, about 8 percent behind the pace last year in nominal dollar terms but 20 to 25 percent behind in volume. Much of the reduction has been in grain imports as improved harvests this year and last have reduced Moscow's requirements. The value of machinery imports appears to be comparable to 1985 as a result of large orders placed last year and the depreciation of the dollar which has raised the cost of purchasing equipment in non-dollar currencies. Soviet commercial borrowing has risen by $3.5 billion through June, with assets in Western banks climbing to a record level of $13.4 billion. Gold sales have also been heavy, reaching an estimated 250 tons through August compared with the 180 tons sold for the whole of 1985. Moscow, benefitting from both higher gold prices and sales, is likely to earn about $4.5 billion in the gold market this year, roughly $2.5 billion above last year's level.

While the Soviet leadership has revealed little about its plans for trade with the West for the 1986-1990 period, we believe that Moscow faces the prospect of imports falling by as much as a third from the 1984 level--in real, depreciated dollars--to levels comparable to the mid-1970s. This estimate allows for some increase in debt--but not by annual increments comparable to 1985 and first half 1986--heavy gold sales, and an $18 average price of Soviet crude oil and oil products during 1986-90. It also reflects our belief that Moscow will be unable to increase substantially non-energy exports, including arms, during this period.

How Moscow will apportion these cutbacks among the various sectors of the economy is as yet uncertain. Its decisions could be somewhat eased by a reduced need for agricultural imports. The improved grain harvests, combined with more efficient feed techniques and low world grain prices, could reduce expenditures on grain by $2-3 billion from the $5.7 billion average in 1981-86. Cutbacks in purchases of machinery and equipment from the West also are likely. The Soviets appear to be intent on limiting the impact of machinery cutbacks, however, by substituting joint ventures for direct purchases which could limit the up-front outlay of hard currency.